Spearheaded by their motivated and able Executive chair in Jeff Bezos, Amazon is one of the world’s leading multinational technology companies, with a main focus on e-commerce, cloud computing and digital streaming; as it captures a 37% market share as the dominant force in retail media as well as a 19% market share (second largest behind Netflix’s’ 21%) in the Streaming Video on Demand (SVoD) market.

Over the last two years (2020,2021), Amazon has been a very success company as it captured around 50% of the entire e-commerce retail market in 2021 and this was arguably largely attributable to the pandemic and it’s lagging effects. As people remained indoors during this period, consumers changed their spending habits and patterns, noticeably in 2020 as Amazon annual financial results showed a 38% increase in their net sales and a 22% increase the following year.

However, the same cannot be said 2022 as this proved to be a tough year for the company leaving it’s performance and health in question. The companies misfortunes are largely linked to the macro environment as soaring inflation and interest rates have halted investment from investors. Not only that, I also believe the company has felt the downside lag of the pandemic as they experience slowing sales (sales increase of 9% in 2022) and predictions of sustained e-commerce growth post the pandemic being far off predictions; the reason being consumers gradually returned to shopping in person and moving away from online retail.

Having conducted an analysis on the company, Amazon’s financial health; though it may not be a cause for concern just yet, overall performance has decreased compared to previous years and the following key areas would be used to further explain the financial health/state of the company;

* Liquidity
* Profitability
* Solvency
* Asset utilization
* Investor ratios

From our Liquidity analysis, we produced the following key ratios for 2021 and 2022 and conclude financial health for Amazon is worse in 2022:

|  |  |  |
| --- | --- | --- |
|  | **2021** | **2022** |
| Current ratio | 1.14 | 0.94 |
| Quick ratio | 0.91 | 0.72 |
| Cash ratio | 0.68 | 0.45 |
| Inventory days | 37.82 | 42.36 |
| Receivable days | 22.31 | 26.72 |
| Payable days | 101.32 | 100.00 |

Based on the current ratio, Amazon has a higher degree of liquidity in 2021 than in 2022. In 2022, the company had $0.94 of current assets able to cover for every $1 of current liabilities compared to $1.14 in 2021. In addition to this the quick ratio fell from 0.91 to 0.72 pointing towards a lesser adequate liquidity(less rapid conversion) once inventories have been removed. Furthermore, we also witness that inventory days have increased for the company in 2022. Pairing this with higher receivable days and lower payable days, from a firms stance there are less efficient and worse off than before as they take longer to sell their produced good, receive cash from sales at a later date and fulfil obligated payments quicker.

As an online marketplace where thousands of vendors are hosted on site, Amazon’s payable days is typically higher than other companies as it is part of its 90-day credit policy. As a result of Amazon’s nature of business, its payable balances are higher than its inventories and receivables where it holds inventory on behalf of its vendors. Therefore, working capital is negative and so is the trading cycle. On a year over year basis the number has worsened in 2019, but can be supported with the argument that Amazon has started its own fulfilment services and is a fast growing company.

Profitability ratios, tell a slightly different story in one area however show an overall trend of a decrease in margins over the year; concluding a financial health decline:

|  |  |  |
| --- | --- | --- |
|  | **2021** | **2022** |
| **Gross margin** | 0.42 | 0.44 |
| **EBITDA margin** | 0.13 | 0.11 |
| **EBIT margin** | 0.05 | 0.02 |
| **Net margin** | 0.07 | (0.01) |

Gross margins increased between 2021 and 2022 indicating Amazons important comparative advantage (38% market share) as Amazon has become a household stapple service and the go to for quick services. However, the remaining ratios paint a different picture as they are all declining between 2021 and 2022. Lower EBIT, EBITDA and Net margins all indicate that Amazon management has been less efficient and effective in their running of the business as the ratios indicate that cost have risen for the business. In context, this could be the result of the current macro-economic factors such as rising inflation and interest rates, which has reduced consumption and investment to Amazon but also largely due to inaccurate future sales forecasts post pandemic.

It is notable that Amazon’s Technology & content and Sales & marketing have seen sharp increases, indicating the heavy spend on AWS and Prime Video content. While the e-commerce segment is seen to be normalizing post the Covid-19 boom, sales reflect the increasing global inflation levels.

|  |  |  |
| --- | --- | --- |
|  | **2021** | **2022** |
| **Debt to Equity (D/E)** | 0.35 | 0.46 |
| **Debt to Assets** | 0.12 | 0.15 |
| **Times interest earned** | 14.04 | 5.72 |
| **FCFE per share** | (3.28) | (3.74) |

Financial leverage based on computed solvency ratios appears to have worsened from the figures below:

D/E increased by 0.11 from 0.35 in 2021 to 0.46 in 2022. While these numbers appear to be relatively comfortable, we still have to recognise that debt now accounts for 46% of equity in comparison to 35% the previous year, whilst debt now finances 15% of assets; a 3% increase from 12% in 2021. Taking a closer look at debt to tangible assets, we saw a 20% increase in this ratio from 2021 to 2022 from 0.25 to 0.3, which means that currently almost 30% of Amazons tangible assets are financed by debt and need to be paid off over time. From an investors perspective these increases in key ratios would inhibit Amazons ability to create a cash surplus than before, detailing a decrease in the financial health of Amazon. However, these rations on a whole are comfortable.

Amazon’s long-term liabilities have been increasing over the years as the company has increased its Financial lease commitments to facilitate the number of new fulfilment centres opened over the last year. Although the long-term debt remain rather steady, financial lease commitments have dramatically increased which has increased the debt service burden as well. However, the company has adequate levels of interest coverage and free cash flow indicating its financial health. However, the increase in the debt level would also mean that the company’s borrowing capacity in future is strained where it might have to pay higher interests to secure more debt.

In relation to Asset utilization, all fingers point to the fact that the company’s financial health has decreased and indicate that Amazon isn’t efficiently using it assets to generate the maximum revenue. Between 2021 and 2022, Asset turnover ratio decreased by roughly 8%, a true indication of a drop in efficiency. This is also aided by a decrease in inventory turnover from 9.65 to 8.62 as well as fixed asset turnover ratio dropping by 13%

|  |  |  |
| --- | --- | --- |
|  | **2021** | **2022** |
| **P/E** | 38.10 | (457.15) |
| **EPS** | 3.24 | (0.27) |
| **ROA** | 0.04 | (0.003) |
| **ROE** | 0.24 | (0.02) |

Amazon has a large portion of goodwill in its asset base, where the Fixed asset turnover is almost three times higher than the total asset turnover. The goodwill and intangibles are manly as a result of acquisitions in addition to the increased R&D spending on AWS which we will have to closely watch for future profitability.

In my opinions, the investor ratios really summarised the current state of amazon as well as it’s financial health. We witness a decrease across all boards from 2021 to 2022, which indicates that investors would be getting less return for their investment if they were to and also indicates that Amazons profitability has decreased of the past year. The company is earning negative earnings per share with negative P/E ratio; ultimately meaning Amazon are losing money.

Furthermore, with negative returns on both their assets(ROA) and equity(ROE); which is largely off putting for investors and pairing that with current low investment due to high interest rates and inflation, this could spell bad news for Amazon.

ROE, ROA and ROCE all are within the health territory, however, have declined compared to previous year. Furthermore, given Amazon’s valuations, one would expect the ratios to be better as there are many other smaller companies with better returns than Amazon, however, it is notable that these valuations are backed by Amazon’s expansion.

<https://www.investopedia.com/terms/p/profitabilityratios.asp>

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